Perspective 86

Quebec

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QUEBEC

ECONOMIC DEVELOPMENT PERSPECTIVE

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1. SUMMARY

After an impressive growth of 5.4 percent in 1984, the Quebec economy expanded by a more modest 4 percent in 1985. Economic activity should increase at a similar rate in 1986.

Despite generally favourable economic conditions, Quebec's demographic and economic decline in relation to the rest of the country has not been reversed, except in the case of employment. On the other hand, the employment recovery has produced mainly low-paying, part-time jobs.

It is thanks to the tertiary sector that employment has recovered and expanded since the recession. Consumer services have benefited most from the shift toward tertiary sector employment. This trend should continue in the coming years at the expense of the primary and secondary sectors.

The manufacturing sector's relatively strong performance since the beginning of the recovery hides profound weaknesses, resulting mainly from the loss of certain economic advantages in Quebec, poor competitiveness, an inadequate industrial structure, slow industrial adjustment and insufficient manufacturing investment aimed at restructuring.

Although the primary sector's share of overall employment is modest and its role in the economy is declining, it remains an important source of economic activity in most regions of Quebec. The main problem confronting several primary industries (agriculture, forestry, mining, fishing) is one of competitiveness.

For these serious structural weaknesses to be overcome and the provincial economy to be revitalized, several challenging problems must be addressed:

* <u>Economic recovery in the Montréal region</u>: Thanks to better economic conditions, the erosion of Montréal's industrial base has abated somewhat. The fact remains, however, that the city's sphere of influence is shrinking to that of a regional centre. Its industrial structure continues to be based on uncompetitive industries and the shift to growth sectors is slow to occur. Montreal's assets, however, make this changeover possible.

* <u>Lagging productivity</u>: Although it has partly caught up with the rest of Canada, Quebec continues to lag significantly behind Ontario in terms of productivity. The challenge will be to revitalize and increase industrial performance by speeding up innovation and the diffusion of new technology.

* Trade liberalization and structural adjustment: Expansion of foreign markets is a matter of survival for a good many Quebec industries. Freer trade with the United States and under GATT will require major adjustment on the part of Quebec companies, especially small businesses, that are currently protected by tariff and non-tariff barriers. Government action will be needed to help carry out this restructuring.

* Strengthening small business: Small business now provides 50 percent of all jobs. Among the major problems facing many small businesses are poor management, underskilled human resources and over-regulation.

* Investment climate: The political and economic climate has improved considerably. The two levels of government are making increasing efforts to co-operate and have done much to create a better investment climate. These efforts must now be sustained.

2. REVIEW OF MAIN INDICATORS

i) Economic Conditions

After reaching an impressive 5.4 percent in 1984, economic growth in Quebec fell slightly to 4.0 percent in 1985, compared with 4.4 percent for Canada as a whole. It should be pointed out that the 1982 recession hit this province harder than the rest of Canada. On the other hand, the recovery has proved to be stronger in Quebec than in other regions and growth in services and investment was particularly strong in 1985.

For the first time since the start of the recovery, the growth of capital spending in Quebec was below the Canadian average in 1985. Over the past two years, Quebec has managed to recover much of the 20 percent share of Canadian capital investment it held in the late 1970s. The rise in manufacturing investment has been remarkable, with increases of 37 percent in 1984 and 23 percent in 1985. The principal industries behind this surge have been primary metals and pulp and paper.

The strongest export performers in 1985 were telecommunications, auto parts, paper and wood. Quebec's main export industries include paper and wood, transportation equipment, primary metals, electrical products and food and beverages. Together, these five industries accounted for close to two-thirds of the province's international exports in 1984.

Employment growth in Quebec has surpassed the national average for three straight years. About 82 000 jobs were added in 1985 and 80 000 the year before. The 1983-85 recovery produced average annual growth of 2.7 percent in employment. Quebec registered a net gain in immigration over emigration in late 1984, the first since 1975. Preliminary figures indicate that this trend is accelerating. The turnaround is due largely to the fairly rapid decline in the number of Quebecers moving to other provinces.

The economic recovery of the past three years will have served mainly to restore the 142 000 jobs lost in 1982. Not until the fall of 1984 did employment exceed the 1981 level, and it was late 1985 before the employment/population ratio surpassed, by a very small margin, its pre-recession level.

Throughout the employment recovery period the unemployment rate declined, to 11.8 percent in 1985, while remaining above its level of the early 1980s. As a percentage of the national average, Quebec's unemployment rate dropped from 122 percent during the 1981-84 period to close to 112 percent in 1985. Despite a lower jobless rate, the number of welfare recipients able to work climbed steadily during the recovery, to nearly 300 000 in 1985.

ii) Forecast

The Conference Board of Canada expects the Quebec economy to grow by about 4.1 percent in 1986, compared with five percent in Ontario and 4.3 percent in Canada as a whole. Private investment will probably remain the principal generator of new economic activity in Quebec. Slower growth is expected in consumer spending, exports to the United States and government spending, the latter because of austerity measures aimed at reducing budget deficits.

The Quebec economy will benefit in 1986 from several major industrial projects, including those of Péchiney, Domtar and Hyundai. Business is expected to continue investing heavily in machinery and equipment in order to modernize and raise productivity. In the economy as a whole, machinery and equipment expenditures have risen far more than investment in new plants over the past two years; they represented 42.3 percent of total Quebec capital investment in 1985, the highest level in twenty years.

Table 1 (Page 21) compares Quebec economic indicators with those of Ontario and Canada.

3. ECONOMIC SITUATION BY SECTOR AND REGION

In spite of the fairly favourable situation, Quebec's demographic and economic weight relative to the rest of Canada continues to decline. Between 1970 and 1985, its population share decreased from 28.2 percent to 25.9 percent, its employment share shrank from 26.9 percent to 24.8 percent and gross domestic product (in current dollars) fell from 24.5 percent to 21.7 percent. Except in the case of population, this erosion has ceased during the recovery.

Transfer payments to individuals represent a growing share of personal income in Quebec, up from 11 percent of personal income per capita in Quebec in 1970 to 18.5 percent in 1985, as against 15.9 percent in Canada as a whole.

Although the birth rate is declining and the population is aging rapidly in Quebec, the proportion of its population aged 65 and over was smaller than in the rest of Canada in 1981 (89 percent of the Canadian average). As elsewhere in the country, an aging population will mean increased fiscal pressure for social programs on both levels of government in the medium and long term.

To explain economic developments in Quebec over the last few years, it is essential to examine the structural changes taking place in its economy (see Tables 2 and 3, Pages 22 and 23) and in its regions (Tables 4.1-4.3, Pages 24-26).

Quebec continues to see a shift in employment from the primary and secondary sectors toward the tertiary sector, a trend which has even picked up speed since the recession. Between 1975 and 1985, job losses in the primary and traditional manufacturing sectors have not been proportionately offset by employment gains in industries with greater value-added such as the "sunrise" manufacturing industries or the more dynamic tertiary activities. Besides, most job creation occurred in the low-value-added job categories of the tertiary sector, especially in consumer-related services. The next section explains in greater detail this trend toward the expansion of tertiary employment in Quebec.

i) Tertiary Sector

a) Expansion of Tertiary Employment

The shift in employment toward the tertiary sector in Quebec is a well-established trend. Over the last ten years, tertiary employment expanded from 64.3 percent of total employment in 1975 to 71.4 percent in 1985. This trend has been accelerating recently, however. The recession and the subsequent recovery resulted in a net loss of 57 000 primary and secondary sector jobs between 1980 and 1985, whereas over the same period 171 000 jobs were created in the tertiary sector, mostly in consumer services (trade, amusement and recreation, personal services, accommodation and food and miscellaneous services).

Growth in tertiary employment is not unique to Quebec. The same pattern is reflected in the rest of Canada. This is a trend that knows no boundaries, as is evidenced by the latest OECD report attributing most job creation in the industrialized countries to the tertiary sector.

The shift in employment toward the service sector is reflected in the growing number of part-time jobs. Between 1980 and 1985, 117 000 part-time jobs were created in Quebec. Conversely, total net job creation stood at 110 000 jobs, meaning that Quebec suffered a net loss of 7000 full-time jobs over this period.

The trend toward part-time employment is particularly marked among young people and adult women. It can be assumed that most of these jobs have little value-added and poor labour market attachment. Therefore, the jobs lost in Quebec during the recession have been recovered in quantity but not in quality.

Over half of all the new jobs created in the tertiary sector as a whole between 1981 and 1985 were created in consumer services and almost a quarter in production services, with the remainder stemming from government and para-public activities. Employment growth in production services and government and para-public services was slowed by the weakness of the primary and secondary sectors and by government budget restrictions. In Quebec, public spending accounts for 49 percent of gross domestic product compared with 41 percent in Canada.

The next few years should see the burgeoning of the tertiary sector continue as a result of modernization plans in the manufacturing sector and a decline in the importance of the resource sector.

In the wake of the 1981-82 recession and with the introduction of deregulation, the transportation sector has had to streamline production, regardless of the mode of transport in question. Long-range plans call for some expansion in employment in this sector.

Given this shift in employment toward the tertiary sector, the province has great potential to increase the productivity and value-added of its tertiary sector thanks to the quality of its scientific, technological and university facilities, as well as its production services. These advantages are discussed in greater detail in the sections on the Montréal region and, to a lesser extent, the Québec City region.

b) Tourism

Tourism plays a leading role in the economic development of Quebec and the growth of its regions, particularly in terms of job creation (85 000 direct jobs). In view of the appreciation of the U.S. dollar against its Canadian counterpart and of American tourists' preferences for different cultural and urban experiences, the Quebec tourist industry can be expected to continue to play a preponderant role in the province's economy.

In addition to its unique cultural flavour, Quebec has various strengths which could be used to better advantage, such as its prime geographic location vis-à-vis the Canadian and northeastern U.S. markets and an excellent transportation system. In addition, major cultural events such as the recent Ramses and Picasso exhibitions, forthcoming events, existing cultural facilities or the planned expansion of museums in the Montréal region are important assets for the revitalization of the province's tourist industry.

Tourism in Quebec is experiencing serious structural problems, however. Its declining competitiveness is due largely to the industry's failure to adapt to changing market conditions. Insufficient investment in accommodation, especially in the moderate-price range, obsolescent recreation facilities, the lack of new, first-rate tourism products, scattered tourist attractions and very keen competition from other countries all work against the industry.

c) Regional Impact

The Québec City and Outaouais regions are heavily reliant on the service sector. Although the Montréal region has a sizable secondary sector, it is also dependent on the service sector.

Montréal, with 56 percent of Quebec's population, weighs heavily in the development of the province's economy. Contraction in manufacturing in Montréal was so severe that overall job losses were not recovered until the end of 1985. The slowness of the recovery in Montréal relative to the rest of the province is due primarily to the stagnating manufacturing sector and the weakening in the long term of the dynamic tertiary activities tied to trade and finance which are losing more and more ground to Toronto. Montréal's problems and the need to revitalize its economy are a major challenge which is discussed in the next chapter.

The tertiary sector is the mainstay of the Québec City region, providing over three-quarters of its employment. The hiring restraints in the provincial public administration will therefore have a particularly significant impact in combination with the problems that have arisen in the primary sector, especially the layoffs in the asbestos mines. In 1985, the region's unemployment rate stood at nine percent and the main sources of job creation in the coming years are likely to stem from research and development, high-technology and tourism.

The Outaouais recorded above-average growth from 1981 to 1984. Along with an increase in the participation rate, which is now the highest in Quebec, the unemployment rate declined from 14 percent in 1984 to 11 percent in 1985. The Outaouais' economy is becoming more heavily dependent than any other region on the tertiary sector. Public administration alone accounts for 25 000 jobs, more than double the figure in manufacturing.

ii) Manufacturing

a) Review by Sector

Over the last three years, the Quebec manufacturing industry has performed well. Since the recovery began, for example, manufacturing gross domestic product (GDP) has risen an average of 4.5 percent a year in real terms. This sector accounts for 19.7 percent of employment in Quebec.

This performance is, however, largely a reflection of the amount of catching-up that has been done and masks the deep-rooted defects in Quebec's industrial base that were so brutally revealed by the 1981-82 recession. Thus, Quebec lost 38 000 manufacturing jobs between 1975 and 1985, whereas Ontario added 130 000. These defects, which stem from the loss of certain comparative advantages in Quebec's economy, take the form primarily of lack of competitiveness, slowness of industry to adjust and insufficient manufacturing investment.

Manufacturing investment in Quebec lagged just when substantial investment was required to address the need to reduce productivity gaps with its main competitors and to restructure the industrial base. Between 1975 and 1985, annual average growth in capital stock in the manufacturing sector contracted sharply in Quebec, at an even faster rate than the Canadian average. Other particular circumstances apart, this marked slowdown seems responsible for the ten-year downward trend in manufacturing employment in Quebec.

Moreover, Quebec's traditional comparative advantages have gradually been eroded. The wage gap that once existed between Quebec and Ontario, which would have helped attract labour-intensive industries to this province, has given way to wage parity. As newly-industrialized countries provide more market competition because of low labour costs and modern technology, Quebec's share of Canadian export manufactures remains around 20 percent, less than its share of total production.

A significant proportion of manufacturing jobs are in extremely uncompetitive industries. Heading the list are the traditional sectors of clothing, textiles, leather and furniture -- industries whose survival is due in no small part to customs tariffs and import quotas. Although the production-cost gap between Quebec and developing countries remains too wide in some sub-sectors, nevertheless there is still a future for firms that can adapt to foreign competition. The most promising segments are the fur, fashion and top-of-the-line clothing industries. Employment gains in these sectors, however, are not likely to compensate for the losses by uncompetitive companies.

Other industries such as petrochemicals, oil refining and shipbuilding are faced with major structural problems. Over-supply is a worldwide problem in the petrochemical industry and the rationalization process initiated in Europe and Japan is now making itself felt in Quebec, particularly in Montréal's East End. Shipbuilding is facing both declining demand and poor international competitiveness.

In the pulp and paper industry, the five-year modernization plan launched a few years ago has stimulated considerable investment. Indeed, the pulp and paper and primary metals sectors are largely responsible for the remarkable growth in manufacturing capital investment in 1984 and 1985. On the other hand, the goal of improvement in plant productivity has resulted in the reduction of the size of the labour force. In this situation, plant modernization has not been enough to make some firms competitive again. In the event of freer trade between Canada and the United States or under GATT, some firms can be expected to carry out further modernization. The ensuing workforce reductions, combined with productivity gains in modernized plants, will lead to significant job losses in these sectors by the end of the decade.

Quebec does, however, have a number of assets on which to base its economic development. The abundance of hydro-electric resources, for example, and cheap electricity rates have encouraged the establishment and modernization of energy-intensive industries. This policy has borne particular fruit in the case of aluminum ingot making and pulp and paper, and is also creating development opportunities in electro-chemistry and electro-metallurgy. In the 1990s, the U.S. market could generate new hydro-electric projects here if Quebec succeeds in signing contracts to export electricity to some of the northeastern states. Falling world oil prices could block these projects, however.

Other opportunities are expected to materialize in the aerospace and urban-transportation equipment industries. The federal government has signed major investment agreements with Pratt & Whitney, Canadair and Spar in promotion of Quebec's aeronautics and aerospace industries.

The manufacture of communications and data-processing equipment is well established in Quebec, which has a number of dynamic companies making the highly specialized products on which the future of this sector depends. Information technologies will make all parts of the economy more productive and more competitive. The establishment of closer ties between Canada and Quebec, on the one hand, and the Francophone countries on the other, could open up new markets and speed up the growth of the communications industries and cultural industries related to high-technology. Also, developing expertise and research capability in biotechnology could attract bio-industries to the province and contribute significantly to strengthening the industrial structure.

b) Regional Impact

The restructuring of industry in Quebec, through which uncompetitive traditional sectors are gradually modernizing or giving way to more technologically advanced sectors, is having an effect throughout the province. The main impact of this rationalization, however, is being felt in the more industrialized regions. The Mauricie/Bois-Francs and Eastern Townships regions fall into this category, as does Montrêal, a special case which will be discussed in greater detail in the next chapter.

The Mauricie/Bois-Francs region, with an unemployment rate of almost 14 percent in 1985, is the most dependent on the secondary sector, even more so than the Montrêal region. Although the traditional industries constitute a large nucleus of the region's manufacturing sector, its industrial structure is fairly diversified, with most industries represented, led by pulp and paper.

Demographic growth in the Eastern Townships from 1981 to 1984 was lower than in the province as a whole and the unemployment rate fell from 13 percent in 1984 to 10 percent in 1985, less than the Quebec average. There have been numerous layoffs in the asbestos mines and more are feared for Asbestos in the next few years as a result of environmental protection restrictions limiting access to international markets, especially those of the U.S. and Europe. The secondary sector is relatively large. Textiles, clothing and footwear provide 38 percent of manufacturing employment, but attempts to diversify into high-technology have met with some success. The pulp and paper industry, where a decline was feared, is also proving stable.

iii) Primary Sector

a) Review by Sector

Although agriculture represented only three percent of total employment in 1985, agriculture-related secondary industries (essentially food and beverages) accounted for 10 percent of manufacturing jobs. Domestic demand is sluggish because of low population growth and relatively high operating costs that are making Quebec less competitive in outside markets. Growth in agriculture will, however, depend on higher productivity and greater diversification and processing of farm products.

Forestry is still a major contributor to the economy in eight of the ten economic regions in Quebec. As with agriculture, its importance is reflected in its impact on manufacturing. In 1983, manufactured forest products accounted for 13 percent of direct employment and more than 22 percent of exports, making them Quebec's leading export manufacturing sector.

This industry is currently faced with structural problems, in spite of excellent market prospects in the longer term. It has not yet recovered from the 1981-82 recession, and lumber is threatened with countervailing duties in its most important market, the United States. In the longer term, competitively priced supplies are expected to pose a problem because of a history of inadequate reforestation and the spruce-budworm epidemic. This industry will have to intensify its efforts to modernize and streamline processing operations and adopt a co-ordinated strategy for the protection and intensive management of Quebec's forests.

Mining has been in a slump since 1980. Between 1980 and 1984, employment fell by more than 24 percent and investment by more than 28 percent. No other industry of such importance has been so severely affected. There are many reasons for the decline. The industry -- and iron, asbestos and copper mining in particular -- has felt the prolonged effects of the recent recession and long-term structural changes. However, there was a considerable increase in production coupled with a decline in employment in 1984, yielding a rise in productivity. The estimates for 1985 call for a slight rise in output.

The mining industry has already adjusted fairly well in the 1980s; only the asbestos sector is expected to suffer major losses in output and employment. Gold is now the leading metal in the province and accounts for almost all mineral exploration in Quebec. The industry has been faced with a saturated market and unfair competition from many developing countries. Its survival depends both on ongoing efforts to improve productivity and the discovery of new products.

Fisheries is of relatively little economic importance to Quebec. Even so, the industry is of paramount importance in a number of regions with few alternative sources of income. Quebec fisheries are experiencing difficulties. Product quality is uneven and unreliable, which limits access to major markets. The fleet, consisting of small coastal vessels, is aging, its modernization is lagging and the technological side of the industry is proving slow to develop.

Most plants have carried out the necessary improvements to comply with the standards set by new Quebec legislation, but few if any of them go beyond the primary processing stage. Only the agencies of the two levels of government are engaged in research and development work. To add to the industry's problems, the U.S. International Trade Commission recently imposed temporary countervailing duties on imports of whole and filleted fresh groundfish.

b) <u>Regional Impact</u>

Quebec has a hundred one-industry towns, half of them wholly dependent on the forestry sector. Contraction in primary activities has already led to the shutdown of some of them, notably Gagnon and Schefferville. Some have sunk into a slump that could call for adjustment policies, as is the case for Thetford Mines. However, the encouragement of workforce transfers to other sectors or to the large urban centres is no longer an ideal solution, given the advent of technology that is speeding up the need for retraining in certain occupations, as well as the high levels of unemployment in the large urban centres.

The communities affected by declining primary activities are mostly in Quebec's resource regions, namely the Lower St. Lawrence/Gaspé, Saguenay/Lac St-Jean, Abitibi/Temiscaming and the North Shore areas.

The Lower St. Lawrence/Gaspé has the highest unemployment rate in the province -- 18 percent in 1985 -- and by far the lowest personal disposable income. Its economy is dependent on the primary sector. Substantial funds are being invested in a number of areas under the Eastern Quebec Development Plan, and close to $100 million has been committed by the federal government to marine, air and rail transport infrastructure, the fishing fleet, forestry, mining, agriculture, tourism and industrial development.

The Saguenay/Lac St-Jean region has the second highest unemployment rate in Quebec after the Lower St. Lawrence/Gaspé. However, demand in the construction industry (the natural gas pipeline, for example) has more than offset the job losses caused by stagnating markets for aluminum and wood and brought the employment rate down by three percentage points in 1985. The relative importance of the secondary sector in the Saguenay/Lac St-Jean, which accounts for one-quarter of all employment there, sets it apart from the other resource regions. There is little diversification. Primary metals, consisting almost entirely of aluminum, provide 40 percent of jobs. The other industries are paper, wood and food and beverages. Consolidation and modernization in the pulp and paper and aluminum industries points to a decline in the demand for workers.

Abitibi/Temiscaming has a relatively high level of unemployment. The primary sector -- mining, forestry and agriculture -- is strongly represented. Manufacturing is based on resource processing, primarily forest resources.

The North Shore is the only region where the number of inhabitants has declined since 1981. The unemployment rate of close to 15 percent in 1985 is down three percentage points from the same period in 1984. Baie Comeau, with a more diversified economy and more solidly based industry, suffered little in the recession because of the $750 million expansion undertaken at the Reynolds aluminum smelter. The region's economic future still depends largely on its forest and mineral resources.

4. MAIN ECONOMIC ISSUES

i) Economic Recovery in the Montréal Region

The Montréal region is extremely important, given that it contains half of the population of Quebec. Its economy was hard hit by the 1981-82 recession, with the region accounting for half of all job losses in Quebec. Whereas the province had made good all of its losses by 1984, Montréal took until the end of 1985 to do so.

It was not until early 1985 that there was any noticeable improvement in economic indicators, with employment on the rise and the unemployment rate falling to 11.7 percent.

The positive net-migration in Quebec since 1984 has mainly benefited the Montréal region. However, even though the recovery has been well under way for some time now, a number of sectors are beset with structural problems, as evidenced by the many plant closures in Montréal East.

First there is the region's demographic situation. The rate of population increase has been lower in Montréal than in any other large Canadian city since 1961 and many of those who have left the Montréal region have moved to Toronto and Western Canada.

The second factor can be seen in the labour market. From 1961 to 1984, employment in Montréal increased by 63 percent, compared with 113 percent in both Toronto and Vancouver and 76 percent in the country as a whole. Since 1977, the regional unemployment rate, traditionally lower than the Canadian rate, has been 1.5 percentage points higher.

Next, there is the phenomenon of the "de-industrialization" of the Montréal economy as the services sector rapidly gains ground. Manufacturing employment rose by a mere 4.2 percent between 1971 and 1984, a performance far inferior to that in the Toronto region. This trend reflects the lack of dynamism in an industrial structure still dominated by traditional industries. Whereas the share held by the traditional sectors (textiles, clothing and footwear, furniture, food and beverages) in the region's manufacturing structure shrank by five percent between 1961 and 1982-83, that held by the modern industries (machinery, printing, transportation equipment, electrical products and chemicals) grew by one percent over the same period.

Whereas manufacturing investment in Montréal was on a par with that in Toronto in 1961, by 1985 it had dropped to only one-half the Toronto level. Moreover, the textiles, clothing and footwear, furniture, petrochemicals and pharmaceuticals industries, which together account for one-third of manufacturing employment in Montréal, all continue to be faced with major structural problems.

Although there has been substantial growth in the "dynamic" tertiary activities in Montréal in the past 20 years, the city lags far behind Toronto in this regard. A number of examples can be cited. Despite a number of laudable attempts to reverse the trend, Montréal has lost much of its role as a major financial centre, with the transfer of many decision-making centres to Toronto. While air transportation has been declining in Montréal, it has grown in other major Canadian centres. The consequence of these declines has been to narrow Montréal's sphere of influence to the purely regional level.

While North American economic activity has been shifting west and south, social and cultural trends in Quebec have changed the face of the province. With the emergence of a strong nationalist movement, the increasing preponderance of the French language in Montréal and the election of a separatist government in 1976, the Montréal business community has been transformed. Many Anglophones have moved westward out of the province. The growing numbers of French-speaking managers and entrepreneurs who have replaced them were naturally drawn during the transition period to traditional sectors directed specifically at the Quebec market.

Taxation and language policy and labour legislation adopted by the former provincial government, along with difficult labour-management relations, have been seen by investors as creating an unfavourable investment climate.

Despite the various problems listed above, Montréal has a number of strengths on which it may draw to ensure its future development.

Although the region's economic base has been eroded, it does have a diversified structure in which the entire manufacturing and tertiary sectors are well represented. Thus, it is possible that the growth sectors will fill the employment gap left by the traditional sectors.

Another of Montréal's strengths lies in its human resources. The four universities in Montréal produce engineers, MBAs, technicians and scientists who help to run its high-technology industries. To list only a few, there are the sectors of aerospace and aeronautics, word processing, and electronics and telecommunications. These industries all have structural, innovative or spinoff effects on the Montréal economy in terms of small business and sub-contracting.

Despite its limited size in the region, the motor tertiary is well represented in various sectors. First, there are the internationally renowned consulting engineering firms of Lavalin, SNC and Monenco, which are among the ten largest such firms in the world. In addition, there are a number of research centres that have a significant impact on regional industry, involved in such fields as biotechnology, office automation, energy, industrial materials research and health sciences, to name only a few of the most important ones. Their activities all have a catalyst effect.

Montréal's dual cultural and linguistic nature is unique in Canada and, indeed, in North America. It has been noted that Montréal sits at the crossroads of Europe and North America and, accordingly, should draw on this asset in order to fully develop its potential. This duality contributes to the quality of life in Montréal in terms of recreation, restaurants and culture.

Montréal is still home to the head offices of various large Canadian companies and the subsidiaries of large multinational firms; more than one hundred at last count. In addition, two non-governmental international organizations are headquartered in Montréal: the International Civil Aviation Association (ICAO) and the International Air Transport Association (IATA).

Various encouraging trends in the business climate have already emerged. Witness the change in attitude among many French-speaking Montréalers toward business, finance and the stock market. The Montréal Stock Exchange has benefited recently from this new enthusiasm and has itself given rise to unusually strong investment activity in Quebec.

New business ventures are also on the rise in Montréal. In addition, today's entrepreneurs have been exploiting their talents throughout the rest of Canada and abroad. There has been an internationalization of attitudes. Moreover, recent and planned changes in taxation, language policy and labour legislation will help to make Montréal increasingly competitive.

Thus, the Montréal region has a number of assets on which to base its recovery. Attempts to speed up industrial adjustment should be pursued by encouraging more productive sectors.

ii) Lagging Productivity

Compared with the rest of Canada, Quebec has made significant productivity gains over the past ten years. While production per employee in Quebec in 1973 was less than 89 percent of the Canadian level, today it stands at 93.4 percent. Quebec ranks fourth in terms of production per employee, behind Alberta, British Columbia and Ontario. While Canada itself ranked second in terms of productivity in 1950, it had fallen to sixth place by 1983. In 1985, production per worker in the Canadian manufacturing sector was 25 percent lower than in the United States.

Despite the fact that it has caught up in part, Quebec continues to lag behind Ontario and Canada as a whole. According to the Quebec Productivity Institute, if the trend since 1971 continues it will take 34 years for labour productivity in Quebec to catch up to Ontario. This gap may be explained, on the one hand, by the more serious under-utilization of human resources in Quebec, reflected in a low participation rate and high unemployment and, on the other, by the lower efficiency of the resources used.

Various factors may be cited to explain the low level of productivity in Quebec, among them:

* The chronic lack of private capital formation. The rate of private, non-residential investment in terms of GDP has been below the Canadian average since 1970.

* Use of the stock of machinery and equipment per worker in Quebec is on average 20 percent lower than in Ontario. Of all the large industries, only forestry and construction, which account for a mere five percent of employment, are ahead of Ontario in terms of labour productivity. Quebec is seriously lagging behind in virtually all other areas of activity.

* The third explanation lies in the industrial structure. Employment in Quebec continues to be concentrated in labour-intensive traditional sectors such as textiles, clothing and footwear. If Ontario's manufacturing industrial structure were transposed onto Quebec, the productivity gap between the two provinces would have fallen in 1982 from 9.7 percent to 4.5 percent.

Other factors may be cited to explain the slowdown in productivity growth in Canada and, to a lesser extent, in Quebec since the oil price shocks of 1973 and 1979:

* Low levels of capacity utilization are coupled with the failure to take advantage of economies of scale. Production equipment has been largely under-utilized as a result of the recent slowdown in economic activity in Canada and Quebec. With the rationalization of operations that has taken place in the manufacturing sector since the 1981-82 recession, however, productivity in Quebec has improved compared with the level in Canada as a whole.

* There has been a deceleration in the re-allocation of resources from less productive activities to more productive ones. Although the relative weight of traditional sectors in the Quebec economy has declined, gains in employment have primarily benefited those sectors with low productivity, such as government and consumer services. Within the manufacturing and tertiary sectors, however, the share held by the "modern" industries and production services has grown very slowly.

* A general slowdown in the rate of adoption of new technology means Quebec lags behind with regard to industrial research and development (R&D) and innovation. Between 1977 and 1982, only one percent of Quebec GDP was invested in research and development, as compared with 1.5 percent in Ontario and 1.2 percent in Canada as a whole. And, Canada itself lags far behind the other industrialized nations, which devote from two to 2.5 percent of their GDP to R&D.

Quebec will have to adapt and improve its industrial performance in order to meet growing international competition. Part of the solution lies in speeding up innovation and in the adoption of new industrial processes. This can be accomplished in part by relying on the public and private research institutes already established in the province in the areas of energy, pulp and paper, industrial materials and processes, medicine, telecommunications, electronics, optics and electro-chemistry.

In spite of this excellent network of technological expertise, much remains to be done to fully exploit its potential, particularly as regards links between universities, research institutes and industry to ensure that research is more closely related to needs and, in particular, to quicken the pace of technology transfer and diffusion.

Agencies are now being formed to make the research skills of educational establishments available to industry. For instance, laboratories with access to different areas of expertise are being set up to solve technical problems referred to them by companies. Bodies that foster links between traditional and high-tech industries could help speed up technology transfer on a national and international level. Consideration also might be given to establishing experimental incubators for high-tech companies that would be managed jointly by universities and the private sector.

Greater emphasis could also be placed on technology diffusion in the services sector, particularly in industries with relatively low labour productivity (socio-cultural, personal and business services, trade and public administration). These industries, which account for close to 60 percent of total employment, offer considerable potential for increasing productivity and, thereby, standards of living.

iii) Trade Liberalization and Structural Adjustment

Evaluating the economic impact of freer trade with the United States and under GATT involves complex analysis of a host of variables, not all of which will be reviewed here. The situation will vary from industry to industry and region to region.

The Quebec manufacturing industry as a whole relies heavily on outside markets, both in other provinces and in foreign countries, which absorb more than 40 percent of production. International exports account for 24 percent of Quebec's GDP, compared with 28 percent for Canada. Quebec's largest customer is the United States, which took a record 75 percent of exports in 1984. Expanding foreign markets is, therefore, essential to the survival of a large part of Quebec manufacturing and of the tertiary sector which is largely dependent on it.

Recent studies conducted by the Economic Council of Canada show that the agreement reached under the Tokyo Round has resulted in significantly lower customs tariffs, particularly for manufactured goods. This has in turn resulted in significant growth in some sectors and in a reduction in the activities and number of firms in declining industries. For each job lost, four others have been created. Workers have been most severely affected in various urban centres in Quebec and Ontario, specifically in single-industry towns. Women and older workers have been the hardest hit.

Should a multilateral agreement be reached under GATT, traditional industries in Quebec will be vulnerable to foreign competition from abroad, in particular from those countries with low labour costs. This would require much greater efforts to adapt the province's economy than would a regional agreement with the United States.

In Quebec, as is the case elsewhere in Canada, critics of trade liberalization with the United States claim that our political, economic and cultural sovereignty would be at risk because Canada would eventually have to align its economic, social and fiscal policies with those of the United States.

Businesses protected by tariff and non-tariff barriers, in particular small and medium-sized companies in Quebec which, by contrast with their larger counterparts, sell only eight percent of their production on foreign markets, will have to change radically in order to adjust to freer trade. Such companies generally have limited marketing plans and very little control over their own markets, and the removal of protective tariffs, which may result in a sudden and massive invasion of their markets, will make them very vulnerable.

Firms and workers in protected industries are concerned about the effects of freer trade with the United States. They are particularly worried about the possible impact on their markets and sources of supply, the adjustment period, protective clauses for promoting the restructuring of less competitive sectors and the necessary government programs for easing the change.

The Canadian Industrial Renewal Board's mandate expires in March, 1986. By that date, it will have spent close to $225 million on modernizing the province's textiles, clothing and footwear industries and on strengthening the economic base of regions heavily dependent on them. Other parts of the province, including resource regions such as Asbestos, are also grappling with structural difficulties, and adjustment and diversification policies are essential to their survival.

Whatever form adjustment policies take -- government assistance to industry or workers, training and retraining, early retirement benefits or mobility assistance -- they must have a sectoral, regional and community dimension.

iv) Strengthening Small Business

Major changes have taken place in Quebec in the past few decades. Its economic base now consists of small and medium-sized companies which account for more than 50 percent of jobs and more than 40 percent of shipments. With the increase in entrepreneurship in Quebec, the process is gaining speed. On a per capita basis, ten times as many companies were incorporated in Quebec in 1982 as in 1955, and the number of new companies being set up now compares favourably with the situation in the United States and the rest of Canada.

Most new companies, however, go under in the first few years of their existence. Though some 10 000 companies have been set up in the secondary sector alone in the last nine years, there has been virtually no change in the overall number of small and medium-sized manufacturing establishments. Because of the mortality rate, 180 jobs have to be created at the outset to obtain a net 100 new jobs. Although Quebec is not unique in this respect, and the situation is even an indication of a degree of dynamism, it does call for a strategic approach to eliminate as many of the reasons for failure as possible.

One of the major problems confronting numerous small and medium-sized companies is poor management. Many of them do not have a marketing plan and have little understanding of the workings of national trade and, consequently, of international markets. They frequently do not have the requisite human and financial resources for innovation, for gaining access to or adopting new technology, or even for taking advantage of potential spin-off from the research and development done by private and public agencies. Their efforts and/or their expertise in the area of improving productivity and product quality are, in many cases, insufficient. Furthermore, their employees often are inadequately trained, making them less competitive.

The two levels of government have agreed to minimize the constraints facing small and medium-sized companies with respect to paperwork, the harmonization of government assistance programs, purchasing policies and tax and other concessions, all with a view to creating a more competitive environment that is more conducive to entrepreneurship.

v) Investment Climate

In recent years, major changes in Quebec's political and social climate have made the situation more conducive to economic recovery. Up to the end of the 1970s, for example, entrepreneurship did not rank as high on the scale of social values as it does now. The feeling then was that the primary responsibility for economic growth lay with government, an attitude that gradually led to the idea of the "welfare state", an idea most people now reject.

The new Quebec government has declared its desire to speed up the changes initiated by the previous government with respect to emphasizing individual initiative and entrepreneurship, privatizing a number of Crown corporations, easing labour legislation, language policy and taxation for individuals and business and gradually reducing the deficit. The government will no longer be an entrepreneur, but a catalyst of economic development. In addition, the government has announced tax exemptions to bolster Montréal's international role.

Quebec has long been known for its union militancy. Attitudes now seem to be undergoing a fundamental change and are becoming more and more pragmatic and open to dialogue. Unions and management are accepting the need to work together within companies to manage technological change.

Federal-provincial relations were extremely strained before the fall of 1984. The two governments are now engaging in a much more open dialogue. Their economic objectives seem to converge and much effort has already been invested in harmonization and co-operation. An umbrella Economic and Regional Development Agreement has been signed, along with eight Canada-Quebec subsidiary agreements valued at $1.2 billion.

The role of the two governments in creating the right kind of climate is critical for the province's economic future, particularly in three areas: the outcome of constitutional talks between Quebec, the federal government and the other provinces; policies related to trade talks with the United States and under GATT; and the gradual elimination of barriers to investment, entrepreneurship and interprovincial trade.

To conclude, the two levels of government have opened many doors in order to improve the investment climate and it is now up to them to maintain the momentum.

ANNEX A

TABLE 1

MAIN ECONOMIC INDICATORS

	1981-1984 (%)	1985 (%)
Gross domestic product		
Rate of growth (constant $)	1.2	4.0
Quebec/Canada (current $)	22.3	21.7
Quebec/Ontario (current $)	60.7	57.8
Population ('000)*	6 438	6 581
Quebec/Canada	26.5	25.9
Quebec/Ontario	74.7	72.6
Net migration (annual)	-10 103	+2 583***
Employment ('000)*	2 726	2 804
Rate of growth	0.2	3.0
Quebec/Canada	24.6	24.8
Quebec/Ontario	64.4	63.7
Participation rate**	61.0	62.2
Quebec/Canada	94.6	95.4
Quebec/Ontario	90.6	91.5
Unemployment rate	12.7	11.8
Quebec/Canada	122.1	112.4
Quebec/Ontario	141.4	147.5
Earned income per capita		
Quebec/Canada	86.0	86.9
Quebec/Ontario	75.2	74.2
Personal disposable income		
Quebec/Canada	93.2	93.3
Quebec/Ontario	85.8	84.7

* Data for 1981.
** The percentage the labour force forms of the civilian population 15 years of age and over.
*** Based on the first three quarters.

Source: Statistics Canada

TABLE 2

TRENDS IN EMPLOYMENT IN QUEBEC BY ECONOMIC SECTOR

	1975 (%)	1985 (%)
Total Primary (1)	4.6	4.5
Secondary		
Traditional sectors (2)	9.3	7.0
Modern sectors (3)	6.1	5.4
Other sectors and construction	14.4	11.7
Total Secondary	29.8	24.1
Tertiary		
Consumer services (4)	25.0	29.3
Production services (5)	17.2	17.6
Government and other services	23.4	24.5
Total Tertiary	65.6	71.4
	100.0	100.0

(1) Agriculture, forestry, hunting and fishing, mining.

(2) Food and beverages, leather, textiles, knitting mills, clothing, furniture.

(3) Printing, machinery, transportation equipment, electrical products, chemicals.

(4) Trade, entertainment and recreation, personal services, accommodation and restaurants, other services.

(5) Transportation, communications and other public services, finance, insurance, real estate and business services.

Source: Statistics Canada, Labour Force Survey

TABLE 3

BREAKDOWN BY SECTOR OF GROSS DOMESTIC PRODUCT

AND EMPLOYMENT

1985

	GDP(1) (%)	Employment(2) (%)
Agriculture	1.5	3.0
Fisheries	--	--
Forestry and trapping	0.6	0.7
Mining	0.7	0.9
Total primary	2.8	4.6
Manufacturing	23.6	19.5
Construction	4.3	4.5
Total secondary	27.9	24.0
Transportation, communications and other utilities	13.8	7.9
Trade	14.2	17.5
Finance, insurance and real estate	13.9	5.6
Community, business and personal services	21.0	33.4
Public administration and defence	6.4	7.0
Total tertiary	69.3	71.4
TOTAL	100.0	100.0

(1) Conference Board of Canada
(2) Statistics Canada

TABLE 4.1

OVERVIEW OF QUEBEC REGIONS

DEMOGRAPHY

	Population June 84	1984/1981 %
RESOURCES REGIONS		
. Gaspé/Lower St.Lawrence	238 452	+1.9
. Saguenay/Lac St-Jean	309 706	+3.0
. Abitibi/Témiscaming	156 612	+2.3
. North Shore/New Quebec	128 748	-1.6
CENTRAL REGIONS		
. Québec	1 053 397	+2.1
. Mauricie/Bois-Francs	451 390	+2.3
. Eastern Townships	242 510	+1.4
. Outaouais	280 929	+2.7
MONTRÉAL REGION	3 691 748	+1.7
PROVINCE OF QUEBEC	6 553 492	+1.8

Source: Statistics Canada and Quebec Bureau of Statistics (1984 estimates)

TABLE 4.2

OVERVIEW OF QUEBEC REGIONS

EMPLOYMENT

	Participation Rate 1985 %	Unemployment 1984 %	Unemployment 1985 %
RESOURCES REGIONS			
• Gaspé/Lower St.Lawrence	53.8	21.6	18.2
• Saguenay/Lac St-Jean	56.2	16.2	15.0
• Abitibi/Témiscaming	57.7	18.9	13.8
• North Shore/New Quebec	63.3	17.7	14.8
CENTRAL REGIONS			
• Québec	61.0	10.9	9.3
• Mauricie/Bois-Francs	58.5	14.9	13.6
• Eastern Townships	61.5	12.7	10.1
• Outaouais	66.8	14.0	10.8
MONTRÉAL REGION	64.1	12.1	11.7
PROVINCE OF QUEBEC	61.9	12.8	11.8

Source: Labour Force Survey (Statistics Canada)

TABLE 4.3

OVERVIEW OF QUEBEC REGIONS

ECONOMIC STRUCTURE

	Employment 1984-1985		
	Primary %	Secondary %	Tertiary %
RESOURCES REGIONS			
• Gaspé/Lower St.Lawrence	14.2	19.0	66.8
• Saguenay/Lac St-Jean	10.7	25.1	64.2
• Abitibi/Témiscaming	17.4	21.1	61.5
• North Shore/New Quebec	14.8	16.1	69.1*
CENTRAL REGIONS			
• Québec	6.0	16.8	77.2
• Mauricie/Bois-Francs	8.7	28.9	62.4
• Eastern Townships	9.3	26.7	64.0
• Outaouais	4.7	15.3	80.0
MONTRÉAL REGION	2.2	27.8	70.0**
PROVINCE OF QUEBEC	4.8	24.8	70.4

Notes: * Employment figures for the North Shore
** Adjusted by Department of Regional Industrial Expansion

Source: Canada Employment and Immigration Commission strategic overview.